

Testimony Summary:
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EPA has almost 20 years of experience designing, operating, and assessing cap and trade programs, most notably, the Acid Rain Program and more recently, the NO_x Budget Trading Program. EPA promulgated two more cap and trade rules in 2005: the Clean Air Interstate Rule and the Clean Air Mercury Rule that will further reduce emissions of SO₂, NO_x, and mercury by up to 70 percent.

Cap and trade is a market-base mechanism that:

- Sets a mandatory cap, or aggregate emissions limit, on a category of sources
- Distributes allowances to those sources equal to the cap
- Requires covered sources to monitor and report all emissions
- Requires covered sources to surrender allowances equal to their emissions
- Allows trading (purchasing or selling) and banking of allowances.

Key principles of cap and trade programs essential to success: Government should focus on the emission reductions goal; keep it simple so it's easily understood; provide certainty; be transparent; and hold itself and industry accountable.

In addition to an emissions-reducing cap and unrestricted trading and banking, key elements of a successful program include:

- Monitoring—accurate measurement and reporting of all emissions from all sources, with complete transparency of data, provides the foundation for ensuring the emission reduction goal and the credibility of the allowance market.
- Allowance distribution—how government distributes allowances (free or by auction) is an important economic and political design decision but does not affect the environmental outcome or the overall costs. It does affect who ultimately pays for the program.
- Implementing legislation—good legislation underpinned the Acid Rain Program's success. There were few legal challenges and none delayed implementation.

The results of the Acid Rain Program and the NO_x Budget Program have been impressive and clearly demonstrate that market-based cap and trade programs are an effective means of achieving broad improvements in air quality by reducing regional and national emissions:

- Compliance with the programs has been greater than 99 percent every year.
- Since 1990, national SO₂ emissions from power plants are down over 40 percent, acid rain is down over 30 percent, and summertime NO_x emissions from power plants and industrial boilers are down over 70 percent.
- The greatest SO₂ emission reductions were achieved in the highest SO₂-emitting states, and trading did not cause "hotspots."
- Human health and environmental benefits were delivered early and broadly.
- Compliance flexibility and allowance trading reduced compliance costs for the Acid Rain Program by more than two-thirds from initial EPA and industry estimates.

Bottom line: a well-designed cap and trade program can be a cost-effective, flexible, and efficient environmental policy instrument for industry and government.